

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 02-20040241
Corporate Income Tax
Tax Period 1999-2001

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ISSUE

1. Corporate Income Tax- Unitary Relationship

Authority: IC 6-8.1-5-1(b); 45 IAC 3.1-1-153; Allied-Signal, Inc. v. Director, Div. of Taxation, 504 U.S. 768 (1992); Container Corp. of America v. Franchise Tax Bd., 463 U.S. 159 (1983); F.W. Woolworth Co. v. Taxation and Revenue Dep't., 458 U.S. 354 (1982); ASARCO, Inc. v. Idaho State Tax Comm'n, 458 U.S. 307 (1982); Exxon Corp. v. Department. of Revenue, 447 U.S. 207 (1980); Mobil Oil Corp. v. Commissioner of Taxes, 445 U.S. 425 (1980).

Taxpayer protests the determination that one of the taxpayer's subsidiaries is not unitary.

STATEMENT OF FACTS

Taxpayer, a food manufacturer, files a consolidated Indiana return. Taxpayer has a business association with an unrelated company. The two parties own a corn mill through a limited partnership. The parties indirectly share ownership in the limited partnership through subsidiary corporations. Taxpayer consists of the parent corporation and two subsidiaries.

The Department conducted an audit and included only the Taxpayer's consolidated group of companies that operated in or had a taxable nexus within Indiana as unitary for purposes of 45 IAC 3.1-1-153. As a result of this determination, the Taxpayer's taxable adjusted gross income increased significantly. The Taxpayer previously treated the income from all of its subsidiaries as unitary and apportioned the income. The taxpayer submitted a protest challenging the audit's determination. The Department held a hearing and now presents this Letter of Findings.

1. Corporate Income Tax- Unitary Relationship

Discussion

To help identify the parties, the department will designate the two subsidiaries as "Subsidiary A" and "Subsidiary B". Both of the subsidiaries, Subsidiary A and Subsidiary B, own interest in a

limited partnership. Subsidiary B is the general partner holding a 1 percent interest. Subsidiary A is a limited partner holding a 79.2 percent interest. An unrelated third company holds a 19.8 percent limited interest in the partnership. The limited partnership distributed its income to the partners based on the partner's ownership percentage.

On audit, the Department took the position that a unitary relationship does not flow through a corporate parent, but rather between the partnership and the corporate partners directly. Using this analysis, the audit review determined Subsidiary B and the limited partnership were unitary and apportioned the income Subsidiary B received from the limited partnership to Indiana. The audit review determined no unitary relationship existed between Subsidiary A and the limited partnership. This determination allowed the Department to allocate Subsidiary A's income from the limited partnership to Indiana in accordance to Subsidiary A's ownership percentage and the limited partnership's Indiana apportionment percentage. The audit review reached its decision, with respect to Subsidiary A, for these reasons: Subsidiary A only derived income from the partnership distributions; its only asset consisted of the limited partnership interest; and its only activity consisted of holding its investment in the partnership. The Department viewed these facts as consistent with a non-unitary business relationship.

Indiana Department of Revenue assessments are prima facie evidence that department's claim for unpaid taxes is valid. IC 6-8.1-5-1(b). The taxpayer has the burden of proving whether the department incorrectly imposed the assessment. Id. The determination of whether or not a unitary relationship exists depends on 45 IAC 3.1-1-153. 45 IAC 3.1-1-153 provides:

(a) A corporate partner's share of profit or loss from a partnership will be included in its federal taxable income and therefore generally subject to the same rules as any other adjusted gross income. (b) If the corporate partner's activities and the partnership's activities constitute a unitary business under established standards, disregarding ownership requirements, the business income of the unitary business attributable to Indiana shall be determined by a three (3) factor formula....

The Supreme Court established the factors to consider in a unitary business analysis. See Allied-Signal, Inc. v. Director, Div. of Taxation, 504 U.S. 768 (1992); Container Corp. of America v. Franchise Tax Bd., 463 U.S. 159 (1983); F.W. Woolworth Co. v. Taxation and Revenue Dep't., 458 U.S. 354 (1982); ASARCO, Inc. v. Idaho State Tax Comm'n, 458 U.S. 307 (1982); Exxon Corp. v. Department of Revenue, 447 U.S. 207 (1980); Mobil Oil Corp. v. Commissioner of Taxes, 445 U.S. 425 (1980). The three factors are: functional integration; centralization of management; and economies of scale. Id. No single factor outweighs the other factors. Id. However, the showing of day-to-day operational control in the partnership indicates the existence of a unitary business relationship. See Allied-Signal, Inc., 504 U.S. at 768; Container Corp. of America, 463 U.S. at 166; ASARCO, Inc., 458 U.S. at 307.

The Taxpayer takes exception to the Department's determination. The taxpayer argues that under the common law definition of unitary business, the subsidiaries and the limited partnership are unitary because the combined group forms a vertically integrated business. According to the Taxpayer, common law defines "unitary business" as "vertically integrated business, either through affiliates or divisions that perform interdependent steps that lead to a finished product". Therefore,

the taxpayer contends that if the Department viewed one member of the vertically integrated business as unitary, then all members of the combined group is unitary.

The taxpayer's interpretation of "unitary business" extends the definition too broadly for 45 IAC 3.1-1-153 purposes. The taxpayer provides no substantive cite for its reliance or use of the common law definition of "unitary business". However, using the analysis established by the Supreme Court cases, the Department must consider each partner in the partnership and determine whether the partner in question can exercise day-to-day operational control. Once the Department completes this examination, then it may apply the factors to further support the existence of a unitary business. Therefore, since Subsidiary A is a limited partner, a presumption exists that limited partners cannot exercise day-to-day operational control in a partnership. Thus, because the Taxpayer has not provided any evidence to rebut this presumption, the audit review correctly determined that Subsidiary A was not unitary with the partnership.

Finding

For the reasons stated above, the department denies the taxpayer's protest.